Hughes as a Wheeler-Dealer

'Unorthodox, Contradictory, Disorganized' Methods

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By Jack Egan
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NEW YORK, April 10—To some, Howard Hughes was the last of his breed, the bucaneer businessman, a throwback to the industrial barons of the turn-of-the-century who controlled their financial fiefs like absolute monarchs.

His empire over the years spanned some of the most volatile, glamorous and profitable sectors of American business—avation, motion pictures, electronics, aerospace, oil drilling, gambling casinos, real estate, broadcasting—and he prided himself on being its sole owner, answerable only to himself, an independent power.

But to others, including many business associates, Howard Hughes was the sui generis eccentric, wheeling and dealing by inscrutable whims, a disembodied voice giving orders over the telephone in the middle of the night, milking the profits of his enterprises to pursue hare-brained schemes, undermining the effectiveness of his managers and jeopardizing the stability of companies that were an integral part of the nation's industrial fabric.

"While in many ways he was a very intelligent person, and he had a very analytical mind, his management practices were at least bordering on the atrocious," recalls Trans World Airlines chairman Charles C. Tillinghast Jr., who was on the opposite side from Hughes in the 12-year legal battle over control of TWA. "He had the effect of impairing the management process more than he helped it."

The story is told of a visit to Hughes in 1953 by then Secretary of the Air Force Harold Talbott to complain of the exodus of some brilliant scientists and engineers from Hughes Aircraft, one of the country's most important defense contractors, because of what they viewed as Hughes' capricious management of the company.

"You personally wrecked a great industrial establishment with gross mismanagement" Talbott reportedly told Hughes. "It was a terrible mistake entrusting the nation's security to an eccentric like you."

Noah Dietrich, the sober accountant who served as Hughes' financial factotum for more than 30 years before a bitter parting in the mid-1950, said "his business methods reflected his life: impulsive, unorthodox, contradictory and disorganized."

And Dietrich, in his personally colored account of his turbulent years with the fabled billionaire, indicated that, more often than not, Hughes had to be saved from his own excess which wound up costing him tens of millions of dollars.

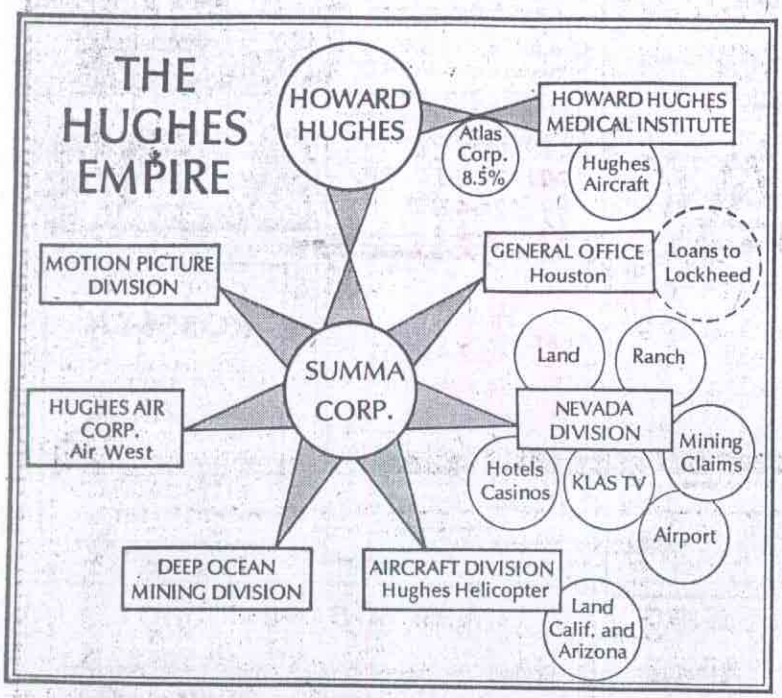
What is undeniable is that, despite eccentricities, Huges parlayed his $325,000 inheritance from his father's oil drilling bit firm, the Hughes Tool Co., into a fortune that at his death last week was variously estimated between $1 billion and $2 billion.

How did he do it? Apparently through a combination of enterprise, luck, good timing, cultivation of high government officials, and by taking maximum advantage of federal tax laws that permitted him to shelter much of his yearly income from the bite of the Internal Revenue Service. Hughes was paying $20,000 a year in taxes when his net worth was approaching $1 billion, according to Dietrich.

Ironically, if no will is found for Hughes, as now seems possible, his empire probably will have to be dismembered and liquidated to come up with the estate taxes which will be levied at a rate in excess of 75 per cent.

The foundation of his fortune was Hughes Tool, known as Toolco, which he inherited when his father died in 1925. Following his father's admonition to go it alone and stay out of partnerships, Hughes at 18 went into court, had himself legally declared an adult, hocked his 50 per cent share of

See HUGHES, F3, Col. 4



By Harold Hoover—The Washington Post
From diagram by Parlos Studio for Fortune magazine

Howard Hughes' empire centered in the end on Summa Corp. and on the Howard Hughes Medical Institute. The relationships of Hughes' varied holdings through Summa Corp. are depicted in the diagram.

HUGHES, From F1

the company for collateral and raised the $325,000 needed to buy out his relatives.

Over the next 48 years, Hughes supposedly set foot in the company's offices only once, finding little in the business to interest him, and he basically left it alone. But it served as his magic money machine.

Toolco had an exclusive patent on a revolutionary three-cone oil and rock drilling bit that was essential to the worldwide petroleum industry and, over a 48-year period, before the company was sold for $150 million in 1973 in a public stock offering, supplied Hughes with $745 million in pre-tax profits. In 1956 alone, Toolco's earnings came to $60 million on revenues of $117 million,for an incredible profit margin of more than 50 per cent.

Avoiding taxes through the reinvestment route, Hughes used the Toolco profits to bankroll his more avid interests: Hollywood and aviation.

Beginning in 1926, the money financed a string of losing motion pictures—though Hughes, in his less reclusive period, seemed as interested in Hollywood's starlets as in the profit potential of the motion picture industry.

Hughes' purchase of RKO in 1948 led to a turbulent period at the studio which ended when he sold RKO for $25 million in 1955, after losing approximately that amount.

Aviation was another matter. This was the area where Hughes left his greatest mark, for good or bad.

An amateur aviator, Hughes set a round-the-world flight record in 1938 of three days, 19 hours and 14 minutes, and established the viability of international aviation. He also started buying into TWA in 1939 with proceeds from Toolco. Separately, he established Hughes Aircraft as a Toolco subsidiary in the 1940s, investing substantial funds to turn it into a high-technology haven after World War II, successfully divining the need for sophisticated electronic gear.

After his confrontation with the Air Force, Hughes spun off Hughes Aircraft in 1953, putting it in a trusteeship with the sole beneficiary being the Howard Hughes Medical Institute, a tax-exempt foundation whose activities are a well-kept secret and which is viewed by many observers as a patent tax dodge.

Hughes Aircraft, however, turned out to be an armageddon of sorts for Hughes, though he emerged largely unscathed, unlike the airline.

Having accumulated 78 per cent of TWA's stock by the late 1950s, Hughes tried to bring TWA into the jet age by unilaterally placing orders for $400 million in planes with various manufacturers, using profits from Toolco.

However, even Toolco couldn't supply TWA with the necessary funds, but Hughes resisted going to Wall Street for financing because he would be required to surrender some control or dilute his ownership—somedthing that was anathema to him.

"The parable of the golden goose held no meaning for Howard," Dietrich recounts. "He was willing to sacrifice Toolco in order to hold on to TWA. Of all his possessions, TWA held a certain mystique for him. He didn't give a damn about the tool company, except as a source of wealth. Hughes Aircraft was an avocation for him, an outlet for his tendency to tinker. RKO was a heady diversion, an opportunity to pursue his sensual enjoyments.

"But TWA was the nearest thing to a passion that this inordinately passionless man possessed," according to Dietrich. Hughes' passion almost led to bankruptcy for TWA, and for himself because of the encumbrances he was being forced to put on Toolco. Finally he agreed to put his TWA stock in trust in 1960 as a condition for getting Wall Street financing for the planes.

This was only the beginning, however, of the largest civil court battle in history, with TWA first gaining a $155 million judgment against Hughes, and then finding it overturned in 1973 by the Supreme Court.

Hughes, in fact, sold Toolco to the public in 1973, raising the $150 million in anticipation that the Supreme Court might rule against him.

He had bailed out of his TWA stock in 1966, however. And, in a stroke of luck or impeccable timing, Hughes managed to get nearly $550 million for his shares, the largest amount of cash that ever had entered an individual's pocket at one time, selling when TWA stock was at $78, close to its all-time high. TWA stock recently has been selling close to $12 a share.

The cash windfall was the base for Hughes' subsequent entry into the Las Vegas gambling scene, where he purchased 7 casinos and thousands of acres of land in the mid-1960s for an estimated $250 million in Nevada holdings.

Hughes' effect on TWA was anything but benefical, according to Tillinghast, who was brought in by company directors when the battle with Hughes was being joined.

TWA's chronic undercapitalization is "a direct inheritance of Hughes," Tillinghast believes. "In 1946, the airline was broke, it had a serious pilot strike and was faced with the real prospect of going down the tubes, and Hughes, in a sense, rescued it with an infusion of money which was enough—but just barely enough—to keep it afloat. In subsequent economic crises, he always did the same thing—always keeping the company undercapitalized and in fragile economic health," as if to maximize its dependence on him.

"One of the things that was also characteristic of Hughes is that he was inordinately interested in the details of aircraft, and undoubtedly made some significant contributions in the design of aircraft," says Tillinghast.

"But so far as we were concerned, it had a very unfortunate effect," he adds, because TWA's airline cockpits, even today, have different instrumentation and configuration than any other airline, requiring costly modification every time an aircraft is bought or sold to make it compatible with the entire fleet.

In the last reclusive years, there

See HUGHES, F10, Col. 6

Hobart Rowen

Tax Reform Need Urgent

HOWARD HUGHES' death is a timely reminder to the Congress of the urgent need for tax reform. The mysterious billionaire's fortune, an estimated $2 billion, could escape taxes up to $1.5 billion if he willed it to the Howard Hughes Medical Institute, a charitable foundation.

If no will turns up, a years-long legal battle between the institute and Hughes' relatives surely is in store.

However that turns out, the Hughes Institute, to which the eccentric industrialist earlier gave 100 per cent of the stock of Hughes Aircraft Co., already has benefited from a multi-million-dollar loophole every year for the last 20 years.

No one suggests that if Howard Hughes succeeded in shielding his enormous fortune from the clutches of the Internal Revenue Service, there had been anything illegal. In fact, it is the very legality of blatant tax avoidance that must be dealt with by Congress, particularly by the tax committees examining reform proposals, and the budget committees dealing with the new and related question of tax expenditures.

The concept of tax expenditures is a useful way of looking at tax loopholes, and shows the degree to which various preferential rates, exclusions, and subsidies are just another form of federal spending.

As to the Hughes case, research by Washington Post investigative reporter Morton Mintz indicates that administrative decisions by the Treasury Department have given the recluse industrialist a special break.

The Treasury classes such operations as his medical research foundation as public instead of private.

Economic Impact

The effect of such a designation is to confer an enormous annual tax concession on the Hughes foundation by reducing the annual amount of required payouts for charitable purposes.

THERE IS a suggestion, but no proof, that favorable rulings for Hughes constituted a political payoff. But even if no special favors had been granted, the cavernous loophole in the law benefiting charitable foundations permits Hughes and others to escape the ordinary tax obligations visited upon ordinary mortals. It is worth noting that Hughes and his colleagues were the only trustees and executive directors of the institute.

Yet, as presidential candidate Morris Udall observes, every time the Congress cranks itself up to consider tax reform, it is inundated by schools, churches and educational institutions begging the legislators not to take away their benefits.

The ingenuity of the loophole-makers knows no bounds. One case was described in testimony last week before the House Ways and Means committee by Thomas J. Reese, director of a public interest taxpayers lobby. He urged support of a bill which would terminate the use of exchange funds to escape paying capital gains.

The story here is that Congress in 1966 closed a loophole which had allowed an investor with a profit in a stock to trade his shares for certain corporate mutual funds, thus entirely avoiding the payment of capital gains.

But an enterprising promoter worked out a way of setting up an exchange fund as a partnership, rather than a corporation. Now, as Reese says, Congress must send a message "to all

See IMPACT, F4, Col. 3